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16 Attorneys for Plaintiffs

17 IN THE UNITED STATES DISTRICT COURT  
18 FOR THE EASTERN DISTRICT OF CALIFORNIA

19 NATIONAL CITY BANK OF INDIANA,  
20 and  
21 NATIONAL CITY MORTGAGE CO.,

22 Plaintiffs,

23 v.

24 DEMETRIOS A. BOUTRIS,  
25 in his official capacity as Commissioner of  
26 the California Department of Corporations,

27 Defendant.

Civil Action No.: S-03-0655 LKK DA

28 NOTICE OF MOTION FOR  
PRELIMINARY INJUNCTION

Submission scheduled for: **BY F**  
Monday, May 5, 2003

TO DEFENDANT AND ITS ATTORNEYS OF RECORD:

Notice is hereby given that Plaintiffs will, and hereby do, move the Court for order granting Plaintiffs a preliminary injunction prohibiting the Commissioner of the California Department of Corporations from: enforcing the California Residential Mortgage Lending Act, Cal. Fin. Code § 50002 *et seq.* (including § 50204(o)), and California Civil Code § 2948.5, against Plaintiffs National City Bank of Indiana, a national banking association, and National City Mortgage Co. ("NCMC"), a wholly owned operating subsidiary of National City Bank from taking any action to prevent or interfere with, either directly or indirectly, Plaintiffs'

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1 rate and amount of interest to be exacted" because the "amount of interest" the mortgage lender  
2 receives is in the hands of the county clerk who records the mortgage, the escrow company, and  
3 the settlement agents. Moreover, the parties cannot contract around the per diem interest  
4 restriction, as they could with the simple interest statute in *Grunbeck*, because (among other  
5 reasons) the pre-closing disclosures required by the federal Truth In Lending Act, 15 U.S.C.  
6 § 1601 *et seq.*, and Regulation Z, 12 C.F.R. part 226, make it impossible for a lender to change  
7 the interest rate set on a loan after closing.

8 By ignoring the fact that the parties cannot contract around the per diem interest  
9 rule, the Commissioner effectively asks this Court to render meaningless the express preemption  
10 on state restrictions on the "amount" of interest charged on residential first mortgages in  
11 § 1735f-7a, in violation of the Supreme Court's teaching that courts must give effect to each  
12 term in a statute. *See, e.g., Duncan v. Walker*, 533 U.S. 167, 174 (2001) (rejecting construction  
13 of a statute that would render statutory term "insignificant, if not wholly superfluous," because  
14 of Court's "duty to give effect, if possible, to every clause and word of a statute") (internal  
15 quotations omitted) (citing cases).

16 Accordingly, the California per diem restriction of California Financial Code  
17 § 50204(o) and California Civil Code § 2948.5 is expressly preempted by DIDMCA and invalid  
18 under the Supremacy Clause.

19 **II. THE BALANCE OF EQUITIES TIPS DECISIVELY IN FAVOR OF A  
20 PRELIMINARY INJUNCTION.**

21 **A. Plaintiffs Will Be Irreparably Harmed If The Commissioner Is Not  
22 Enjoined From Asserting Licensing, Regulatory, Supervisory, Examination,  
23 And Enforcement Authority Over NCMC.**

24 After a recent audit and examination, the Commissioner alleged that NCMC  
25 violated the California per diem restriction by charging interest on residential mortgage loans  
26 prior to one day before the recording of the mortgage by, for example, charging interest from  
27 the date of disbursement even though the recording of the mortgage did not occur until several  
28 days later. Knight Decl. ¶¶ 8, 9. The Commissioner is now seeking to require NCMC to  
comply with the state's per diem interest restriction both prospectively and retroactively by  
forcing NCMC to undertake a manual audit of more than 150,000 mortgage loan files, which,

1 based on current estimates, would cost NCMC in excess of \$4 million. *Id.* ¶¶ 9, 10. There is no  
2 means by which Plaintiffs can recover the amounts expended on the manual audit on which  
3 Commissioner insists if Plaintiffs ultimately prevail on the merits of this suit. *Id.* ¶ 11.

4 Further, as a result of the California per diem restriction, NCMC presently loses  
5 significant revenues each month in interest charges on the interest-free mortgage loans it must  
6 make for the time between the date on which loan funds are disbursed and the day before the  
7 date on which the mortgage is recorded. *Id.* ¶ 12. NCMC would be barred from ever collecting  
8 these sums if the California per diem rule continues in effect. *Id.* As the *Bank of America*  
9 district court found in issuing a preliminary injunction against two California cities that had  
10 enacted legislation to ban ATM fees:

11 [T]housands of dollars of revenue will be lost each month, and  
12 plaintiffs have no feasible means of later recovering fees from  
13 individuals who use the machines without paying these fees.  
There is no question that such harm is significant.

14 Preliminary Injunction Order in *Bank of America, N.A. v. City and County of San Francisco*,  
15 No. C 99 4817 VRW, 1999 WL 33429989, at \*4 (N.D. Cal. Nov. 15, 1999) (Apex F), *aff'd*, 215  
16 F.2d 1332, 2000 WL 340773 (9th Cir. Mar. 31, 2000). The same point is applicable here.<sup>8</sup>

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18  
19 <sup>8</sup> Further, the California residential mortgage market accounts for a significant share of  
20 NCMC's annual loan production volume, and generates tens of millions of dollars each year in  
21 gross revenue for NCMC. Knight Decl. ¶ 5. Plaintiffs know of no way that they can recover  
22 these revenues if they ultimately succeed on the merits of this action but are impeded by the  
Commissioner from continuing NCMC's business operations in California for some period of  
time before they obtain a favorable final decision from this Court. *Id.* ¶ 12.

23 In this regard, National City Bank also will be irreparably harmed because the  
24 Commissioner's ongoing licensing, regulation, supervision, and examination powers, and  
25 especially the specter of his enforcement actions, threaten to disrupt substantially the bulk of the  
26 Bank's residential mortgage lending and servicing business in California, which the Bank  
27 undertakes through NCMC. Stitle Decl. ¶ 4. The Bank knows of no way it could transfer  
28 NCMC's business to the Bank itself without experiencing significant disruption in its mortgage  
lending and servicing operations, as well as incurring considerable expense. *Id.* Moreover, the  
Bank knows of no way that it can recover these revenues and additional expenses if the Court  
ultimately decides in Plaintiffs' favor on the merits of this action. *Id.* ¶¶ 4, 7.

1           **B.     The Public Will Be Protected During The Pendency Of A Preliminary**  
2           **Injunction.**

3           Conversely, California itself would suffer no irreparable harm from the  
4           injunction. "Since Congress expressly preempted this area of regulation, the state[] [will] not  
5           [be] injured by the [preliminary] injunction." *Trans World Airlines, Inc. v. Mattox*, 897 F.2d  
6           773, 784 (5th Cir. 1990), *aff'd in part, rev'd in part on other grounds*, 504 U.S. 374 (1992).<sup>9</sup>  
7           Nor will its citizens.

8           First, the public will be protected, because, as noted above, NCMC remains  
9           subject to the ongoing federal licensing, regulation, supervision, examination, and enforcement  
10          authority of the OCC. Further, the OCC has plenary authority to enforce federal and non-  
11          preempted state laws against NCMC as well as against its parent National City Bank. See 12  
12          C.F.R. § 5.34.

13          Second, to allow recovery of any interest charges received in violation of the per  
14          diem restriction during the pendency of a preliminary injunction should the California per diem  
15          restriction ultimately be upheld by this Court in a final decision, NCMC will maintain  
16          appropriate records of their mortgage disbursement transactions during such time and refund the  
17          amounts overpaid to mortgagors as described in the attached Declarations if the restriction is  
18          ultimately upheld by this Court. Knight Decl. ¶ 13; Stitle Decl. ¶ 8. Given this refund  
19          arrangement, the balance of equities tips decidedly in Plaintiffs' favor: A denial of the  
20          injunction would lead to clear-cut, large, irreparable losses that Plaintiffs could never recover  
21          even if they prevail on the merits; by contrast, customers would be reimbursed if the per diem  
22          restriction is ultimately upheld.

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<sup>9</sup>          "[I]t is undeniable that the public interest weighs in favor of enjoining the government  
26          from violating federal law." *Berne Corp. v. Government of Virgin Islands*, 120 F. Supp. 2d 52  
27          537 (D.V.I. 2000).  
28

## CONCLUSION

1  
2 As this Court held in *Wells Fargo*, "a serious federal and state regulatory dispute  
3 is involved and the balance of hardships tips sharply in Plaintiffs' favor on the issue that the  
4 National Bank Act prohibits the Commissioner from exercising visitatorial powers over  
5 Plaintiffs." *Wells Fargo* PI Order at 14 (2003 WL 1220131, at \*7). Accordingly, the Court  
6 preliminarily enjoined the Commissioner from exercising visitatorial powers over Plaintiffs.

7 Similarly, in their case, Plaintiffs have demonstrated a strong likelihood of  
8 success on the merits. Plaintiffs also have shown that they face irreparable injury if the  
9 Commissioner is not preliminary enjoined from enforcing the California per diem restriction  
10 and the California licensing, regulation, supervision, and examinations provisions, and from  
11 taking any enforcement actions against NCMC, whereas neither the public nor the state faces  
12 comparable harm if an injunction is issued. Therefore, Plaintiffs respectfully request that this  
13 Court grant their Motion for a Preliminary Injunction, as the Court has already done in *Wells*  
14 *Fargo*.<sup>10</sup>

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23 <sup>10</sup> Should the Commissioner, before this Court has an opportunity to rule on Plaintiffs'  
24 preliminary injunction motion, attempt to prevent Plaintiffs from continuing to make and servi  
25 mortgage loans in California pursuant to their federal licenses or otherwise attempt to exercise  
26 visitatorial powers over NCMC, Plaintiffs may be compelled to file a motion for a temporary  
27 restraining order, pending a ruling on Plaintiffs' preliminary injunction motion, for the same  
28 relief sought here - i.e., to enjoin the Commissioner from exercising visitatorial powers over  
NCMC or from otherwise preventing or interfering with Plaintiffs' business operations in  
California.

Apr-03-03

12:31pm

From-Covington & Burling San Francisco

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T-152 P.035/102 F-062

Respectfully submitted,

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ATTORNEYS FOR PLAINTIFFS

Dated: April 3, 2003

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21 and  
22 NATIONAL CITY MORTGAGE CO.,

23 Plaintiffs,

24 v.

25 DEMETRIOS A. BOUTRIS,  
26 in his official capacity as Commissioner of  
27 the California Department of Corporations,

28 Defendant.

Civil Action No.: S 03-0655 LKK DAD

DECLARATION OF STEPHEN A.  
STITLE IN SUPPORT OF PLAINTIFFS'  
MOTION FOR PRELIMINARY  
INJUNCTION **BY FAX**

I, Stephen A. Stitle, do hereby declare and say:

1. I am chairman of the board, president, and chief executive officer of National City Bank of Indiana ("National City Bank" or the "Bank"). I have served as president and chief executive officer since July 20, 1999, and have served on the Bank's board of directors since 1990. I have been chairman of the board since January 1, 1996. My duties at National City Bank include overseeing all aspects of the Bank's operations and performance.

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1 The statements in this declaration are based upon my personal knowledge, on a review of the  
2 Bank's records, and on information provided at my request by persons within the company as to  
3 matters within their areas of responsibility. These statements are true and correct to the best of  
4 my knowledge and belief.

5           2. National City Bank is a federally chartered national bank that is organized  
6 and exists under the National Bank Act. As a nationally chartered bank, National City Bank is  
7 empowered to loan money and to do so through an operating subsidiary if it so chooses.  
8 Pursuant to the National Bank Act and implementing regulations promulgated by the Office of  
9 the Comptroller of the Currency ("OCC"), National City Bank wholly owns and operates  
10 National City Mortgage Co. ("NCMC") as an operating subsidiary to conduct residential  
11 mortgage lending on its behalf.

12           3. NCMC functions as a separately incorporated department or division of  
13 National City Bank, exercising the bank's federally authorized lending powers. Both National  
14 City Bank and NCMC are subject to ongoing regulation, supervision, examination, and  
15 enforcement by the OCC with respect to compliance with both federal and non-preempted state  
16 laws.

17           4. NCMC was established as a subsidiary for the purpose of conducting  
18 residential mortgage lending. It currently conducts the majority of the Bank's residential  
19 mortgage lending throughout the United States, including in California. The subsidiary  
20 structure is advantageous for National City Bank because, among other reasons, it allows the  
21 Bank to focus the subsidiary, with its separate sales force, processing system, and business  
22 model, entirely on an important product line: residential mortgage lending. The Bank knows of  
23 no way it could transfer NCMC's business to the Bank itself without experiencing significant  
24 disruption in its mortgage lending operations and incurring considerable expense. The Bank  
25 also knows of no way that it could recover these additional expenses.

26           5. Despite the fact that National City Bank is federally regulated, the  
27 Commissioner of the California Department of Corporations ("the Commissioner") takes the  
28 position that its operating subsidiary, NCMC, is required to comply with a California restriction



1 on mortgage interest that may be charged to consumers (the "per diem restriction"). This  
2 restriction appears in the California Residential Mortgage Lending Act ("California RMLA").  
3 Moreover, the Commissioner has asserted authority to regulate, supervise, examine, and enforce  
4 federal and state laws against NCMC under the California RMLA.

5           6. If these state laws apply, and if the Commissioner is not enjoined from  
6 enforcing them, they would directly obstruct and impede the Bank's ability to exercise lending  
7 power through an operating subsidiary. This overlapping and inconsistent federal and state  
8 regulation, supervision, examination, and enforcement authority against National City Bank's  
9 operating subsidiary may force the Bank to bring national-bank activities that it now conducts in  
10 NCMC back up into the Bank itself, and thus significantly interfere with the Bank's authority  
11 under the OCC's regulations to establish, own, and operate an operating subsidiary. In any  
12 event, the state restrictions and the Commissioner's assertion of regulatory, supervisory,  
13 examination, and enforcement authority over NCMC significantly interferes with the Bank's  
14 ability to engage in residential mortgage lending itself through an operating subsidiary.

15           7. If the Commissioner is not enjoined from enforcing the per diem interest  
16 restriction, and from otherwise exercising his regulatory, supervisory, examination, and  
17 enforcement authority over NCMC, NCMC will lose significant revenues each month in interest  
18 charges on mortgages for the time between disbursement of loan funds and the recording of the  
19 corresponding mortgages to the extent such time periods exceed one day. NCMC would be  
20 barred from ever collecting these revenues if the California per diem restriction is permitted to  
21 continue in effect, thus causing further irreparable harm to both entities.

22           8. Should a preliminary injunction be granted, NCMC would maintain the  
23 information necessary to calculate any required refund to the consumer and would issue refunds  
24 as appropriate should the per diem restriction be upheld on final adjudication of the merits by  
25 this Court.

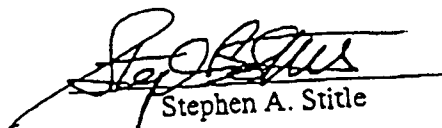
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I declare under penalty of perjury that the foregoing is true and correct.

Executed on 2d day of April, 2003.

  
Stephen A. Stitle

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23 v.

24 DEMETRIOS A. BOUTRIS,  
25 in his official capacity as Commissioner of  
26 the California Department of Corporations,

27 Defendant.

Civil Action No.: S 03-0655 LKK I

**BY F.**

DECLARATION OF  
LEO E. KNIGHT, JR.  
IN SUPPORT OF PLAINTIFFS'  
MOTION FOR PRELIMINARY  
INJUNCTION

28 I, Leo E. Knight, Jr., do hereby declare and say:

1. I am chairman and chief executive officer of National City Mortgage Co. ("NCMC"). I have been employed by NCMC and its predecessor, Shawmut Mortgage Corp., in various capacities since May 1, 1974, including serving as chief executive officer since 1981. My current duties include overseeing all aspects of NCMC's operations and performance. The statements in this declaration are based upon my personal knowledge, a review of the records of NCMC, and information provided at my request by persons within the company as to matters

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1 within their areas of responsibility, and they are true and correct to the best of my knowledge  
2 and belief.

3 2. NCMC is a wholly owned operating subsidiary of National City Bank of  
4 Indiana ("National City Bank"), a federally chartered national bank that is organized and exists  
5 under the National Bank Act. Pursuant to the National Bank Act and implementing regulations  
6 promulgated by the Office of the Comptroller of the Currency ("OCC"), National City Bank has  
7 established, wholly owns, and operates NCMC as an operating subsidiary to conduct the  
8 majority of National City Bank's residential mortgage lending throughout the United States,  
9 including in California.

10 3. NCMC functions as a separately incorporated department or division of  
11 National City Bank, exercising the bank's federally authorized lending powers. As an operating  
12 subsidiary of a national bank, NCMC is subject to ongoing licensing, regulation, supervision,  
13 examination, and enforcement by the OCC with respect to its compliance with both federal and  
14 non-preempted state laws. In this regard, NCMC has been examined by the OCC since  
15 it became an operating subsidiary of National City Bank on March 1, 1998.

16 4. Nearly all the mortgages that NCMC makes are first liens secured by  
17 residential real property, and most have been made after March 31, 1980. NCMC makes  
18 residential real estate loans aggregating more than \$1 million per year. NCMC is a "creditor" as  
19 that term is defined in the Truth In Lending Act.

20 5. California accounts for a significant portion of NCMC's business,  
21 generating tens of millions of dollars a year in gross revenue. NCMC originates billions of  
22 dollars a year in California residential mortgage loans, and services billions of dollars annually  
23 in California residential mortgage loans.

24 6. Pursuant to the California Residential Mortgage Lending Act ("California  
25 RMLA"), NCMC is required to maintain a residential mortgage lending and servicing license  
26 issued by the Commissioner in order to engage in the residential mortgage business in  
27 California. At the time NCMC received this license, in July 1997, it was not an operating  
28 subsidiary of a national bank as it is now; it was a subsidiary of National City Bank's holding

1 company, National City Corporation. NCMC did not become an operating subsidiary of a  
2 national bank, National City Bank, until March 1, 1998.

3 7. In addition to requiring NCMC to secure a license, the Commissioner has  
4 asserted broad regulatory, supervisory, examination, and enforcement authority over NCMC,  
5 including authority to conduct audits and examinations of NCMC and to require NCMC to file  
6 reports with his office.

7 8. After an August 2002 audit and examination, the Commissioner asserted  
8 that NCMC had violated the California "per diem restriction." The Commissioner asserted that  
9 NCMC had violated the per diem restriction by charging interest for more than one day prior to  
10 the recordation of the mortgage.

11 9. The Commissioner has demanded that NCMC comply with the state's per  
12 diem interest restriction both prospectively and retroactively, including a demand that NCMC  
13 undertake a full audit of all files of mortgage loans that NCMC has made since August 2, 2000.  
14 The Commissioner insists that NCMC refund all per diem interest in excess of one day prior to  
15 the recording of the mortgage, regardless of when the loan transaction was consummated (with  
16 certain limited exceptions). The Commissioner has also demanded that NCMC pay 10 percent  
17 interest on such refunds.

18 10. Since August 2, 2000, NCMC has originated 150,000 to 180,000  
19 mortgage loans in California. To comply with the Commissioner's demands, NCMC would be  
20 required to conduct a manual audit of its files, retrieving each file from storage and reviewing it,  
21 in order to determine which loans are covered by the Commissioner's demand. Such a manual  
22 audit would be required because NCMC lacks any automated means to identify the universe of  
23 loans with which the Commissioner has taken issue. Such an audit would cost more than \$4  
24 million, thus imposing a significant financial burden on NCMC.

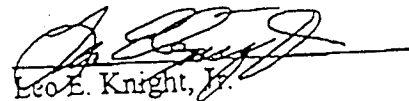
25 11. NCMC is not aware of any means by which it could recover the costs of  
26 performing the manual audit demanded by the Commissioner if the state statutes and regulations  
27 by which the Commissioner purports to act are later found to be unconstitutional or otherwise  
28 unlawful. Thus, NCMC will suffer irreparable harm if the per diem restriction, as well as the

1 Commissioner's authority to license, regulate, supervise, examine, and enforce laws against  
2 NCMC pursuant to state law, are not enjoined.

3 12. Additionally, insofar as NCMC currently is subject to compliance with  
4 the per diem interest restriction, NCMC steadily loses significant revenue by not being able to  
5 charge interest on mortgages for the total time that elapses, when such time exceeds one day,  
6 between the consummation of the loan and the recording of the corresponding mortgage.  
7 NCMC would be barred from ever collecting these revenues if the California per diem  
8 restriction continues in effect, thus causing further irreparable injury to NCMC.

9 13. Should a preliminary injunction be granted, NCMC would maintain the  
10 information necessary to calculate any required refund to the consumer and would issue refunds  
11 as appropriate should the per diem restriction be upheld on final adjudication of the merits by  
12 this Court.

13 I declare under penalty of perjury that the foregoing is true and correct.  
14 Executed on the thirty-first day of March, 2003.


15   
16 Leo E. Knight, Jr.

1 business operations in California (including taking any actions to impose penalties on  
2 Plaintiffs); and from otherwise exercising visitatorial powers over Plaintiffs.

3 The Motion is based upon this Notice of Motion, the accompanying Plaintiffs'  
4 Motion for Preliminary Injunction, and Memorandum in Support of Plaintiffs' Motion for  
5 Preliminary Injunction, the Declarations of Stephen A. Stille and Leo E. Knight, Jr., all  
6 pleadings and other papers on file in this action, and upon such other matters as may be  
7 presented to the Court at the time of submission.

8 Plaintiffs' Motion for Preliminary Injunction shall be submitted on the Court's  
9 civil law and motions calendar for Monday, May 5, 2003 or at such earlier date that the Court  
10 may set. No hearing is requested.

11 Dated: April 3, 2003

  
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22 versus

23 DEMETRIOS A. BOUTRIS,  
 24 in his official capacity as Commissioner of the  
 25 California Department of Corporations,

26 Defendant.

Civil Action No. S-03-0655 LKK DAD

PLAINTIFFS' MOTION FOR  
 PRELIMINARY INJUNCTION

Submission scheduled for  
 Monday, May 5, 2003

**BY FAX**

27 Pursuant to Rule 65 of the Federal Rules of Civil Procedure, Plaintiffs National  
 28 City Bank of Indiana, and National City Mortgage Co. ("NCMC"), respectfully request that the  
 Court enter a preliminary injunction pending final resolution of this action enjoining Defendant  
 and his agents from enforcing or taking any action to enforce the California Residential  
 Mortgage Lending Act, Cal. Fin. Code § 50002 *et seq.* (including § 50204(o)), and California  
 Civ. Code § 2948.5, against Plaintiffs; from taking any action to prevent or interfere with, either  
 directly or indirectly, Plaintiffs' business operations in California (including taking any action  
 to impose penalties on Plaintiffs); and from otherwise exercising visitatorial powers over  
 Plaintiffs.

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1 This motion has been noticed for the Court's May 5, 2003, civil law and motions  
2 calendar. No hearing is requested. Plaintiffs do not believe that oral testimony of witnesses is  
3 required for a decision on this motion.

4 As set forth in the memorandum and declarations filed in support of this motion  
5 and in the Complaint, this case presents the same legal issues underlying this Court's grant of a  
6 preliminary injunction against Defendant in *Wells Fargo Bank, N.A. v. Boutris*, No. 03-0157  
7 GEB JFM. This case is related to *Wells Fargo*. Accordingly, this Court should grant Plaintiffs  
8 in this case a preliminary injunction for the same reasons it issued one in *Wells Fargo*.

9 Like the *Wells Fargo* Plaintiffs, Plaintiffs here meet all of the requirements for  
10 the issuance of a preliminary injunction. Specifically, the Defendant's asserted licensing,  
11 regulatory, supervisory, examination, and enforcement authority over NCMC, an operating  
12 subsidiary of a federally chartered bank, is preempted by the National Bank Act, 12 U.S.C. § 21  
13 *et seq.*, and regulations adopted by the Office of the Comptroller of the Currency ("OCC")  
14 pursuant to that Act. Moreover, the substantive state interest charge restriction that Defendant is  
15 attempting to impose on Plaintiffs (the so-called "per diem restriction") is expressly preempted  
16 by the federal Depository Institutions Deregulation and Monetary Control Act of 1980, 12  
17 U.S.C. § 1735f-7a(2)(1).

18 If the Defendant is permitted to continue to demand Plaintiffs' compliance with  
19 the per diem restriction, as well as to assert licensing, regulatory, supervisory, examination, and  
20 enforcement authority over Plaintiff NCMC, Plaintiffs will be irreparably harmed, even if these  
21 state laws are subsequently held by this or another Court to be preempted. Defendant  
22 Commissioner is presently demanding that NCMC conduct a manual audit of all of its mortgage  
23 loan files since 2000. This audit of more than 150,000 loans will cost Plaintiffs at least \$4  
24 million to conduct, not including possible payments to borrowers. This money could never be  
25 recovered should Plaintiffs ultimately prevail on the merits of this case.

26 Conversely, because Plaintiffs will reimburse affected customers if the per diem  
27 restriction is ultimately upheld, there would be no corresponding losses suffered by the public  
28 by virtue of grant of an injunction.

1 Further, because both Plaintiffs are subject to ongoing, exclusive licensing,  
2 regulation, supervision, examination, and enforcement by the federal Office of the Comptroller  
3 of the Currency, there is no danger that NCMC's activities will remain unregulated in  
4 California, or that NCMC will operate in an unsafe or unsound manner.

5 Accordingly, Plaintiffs respectfully request that the Court issue a preliminary  
6 injunction in Plaintiffs' favor against Defendant, as it did in *Wells Fargo*, pending a final  
7 resolution of the merits of this case.

8 Respectfully submitted,

9  
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26 Dated: April 3, 2003  
27  
28

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16 Attorneys for Plaintiffs

17 IN THE UNITED STATES DISTRICT COURT  
18 FOR THE EASTERN DISTRICT OF CALIFORNIA

19 NATIONAL CITY BANK OF INDIANA, and  
20 NATIONAL CITY MORTGAGE CO.,

21 Plaintiffs,

22 versus

23 DEMETRIOS A. BOUTRIS,  
24 in his official capacity as Commissioner of the  
25 California Department of Corporations,

26 Defendant.

Civil Action No. S-03-0655 LKK DAD

**BY FAX**

[PROPOSED] ORDER GRANTING  
PLAINTIFFS' MOTION FOR  
PRELIMINARY INJUNCTION

27 TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:

28 The Court, pursuant to Rule 65 of the Federal Rules of Civil Procedure, and after  
reading the parties' briefs, hereby directs that the Plaintiffs' Motion for Preliminary Injunction  
against Defendant is GRANTED pending final resolution of this action.

Specifically, the Court ORDERS the following:

Pending further order of this Court, Defendant and his agents are hereby  
ENJOINED and shall CEASE and DESIST from enforcing or taking any action to enforce the  
California Residential Mortgage Lending Act, California Fin. Code § 50002 *et seq.* (including  
§ 50204(o)), and California Civil Code § 2948.5, against Plaintiffs; from taking any action to

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1 prevent or interfere with, either directly or indirectly, Plaintiffs' business operations in  
2 California (including taking any actions to impose penalties on Plaintiffs); and from otherwise  
3 exercising visitorial powers over Plaintiffs.

4 It is further ORDERED that Plaintiffs shall post a bond with the Court in the  
5 amount of \$10,000 as security.

6 IT IS SO ORDERED.

7  
8 Dated: \_\_\_\_\_, 2003

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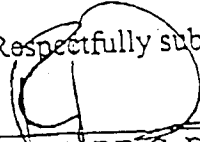
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28

United States District Judge

Respectfully submitted,

  
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17 IN THE UNITED STATES DISTRICT COURT  
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20 NATIONAL CITY BANK OF INDIANA, and  
21 NATIONAL CITY MORTGAGE CO.,

22 Plaintiffs,

23 versus

24 DEMETRIOS A. BOUTRIS,  
25 in his official capacity as Commissioner of the  
26 California Department of Corporations,

27 Defendant.  
28

Civil Action No. S-03-0655 LKK DAD

**MEMORANDUM OF POINTS AND  
AUTHORITIES IN SUPPORT OF  
PLAINTIFFS' MOTION FOR  
PRELIMINARY INJUNCTION**

Submission scheduled for:  
May 5, 2003

**BY FAX**

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1 CONCLUSION..... 20

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## INTRODUCTION

This case is identical in all material respects to *Wells Fargo Bank, N.A. v. Boutris*, No. 03-0157 GEB JFM, in which this Court, on March 10, 2003, issued a preliminary injunction against Defendant Commissioner of the California Department of Corporations ("Commissioner"). See \_\_\_\_ F. Supp. 2d \_\_\_\_, 2003 WL 1220131 (E.D. Cal. Mar. 10, 2003) (Apx A).<sup>1</sup> Plaintiffs seek the same injunctive relief as did the *Wells Fargo* Plaintiffs. And the Plaintiffs do so on the same grounds: The Commissioner is asserting licensing, regulatory, supervisory, examination, and enforcement authority over Plaintiff National City Mortgage Co. ("NCMC"), an operating subsidiary of Plaintiff National City Bank of Indiana ("National City Bank"), and Plaintiffs will thereby suffer irreparable harm because NCMC, as an operating subsidiary of a national bank, is subject to exclusive federal licensing, regulation, supervision, examination, and enforcement by the Office of the Comptroller of the Currency ("OCC"). The Commissioner's assertion of authority over NCMC interferes with the exclusive visitatorial powers accorded to the OCC over national banks and their operating subsidiaries pursuant to the National Bank Act and other federal banking laws, and conflicts with the federal powers of national banks, including National City Bank, to conduct their federal banking activities, such as mortgage lending in this case, through operating subsidiaries. Accordingly, this Court held in *Wells Fargo*, under virtually identical circumstances, that "the Commissioner is preliminarily enjoined from exercising visitatorial powers over Plaintiffs or from otherwise preventing [Wells Fargo Home Mortgage Inc, as an operating subsidiary of a national bank,] from operating in California." PI Order at 15 (2003 WL 1220131, at \*8). The Court should issue a similar injunction in this case.

As in *Wells Fargo*, Plaintiffs also seek preliminary injunctive relief from this Court based on the immediate demand of the California Department of Corporations ("DOC").

---

<sup>1</sup> The Appendix ("Apx") attached to the end of this Memorandum contains copies of the unreported cases and regulatory materials cited herein.

1 through Defendant Commissioner, that NCMC conduct a manual audit of more than 150,000  
2 mortgage loan files in order to identify possible instances of non-compliance with a state  
3 restriction that is expressly preempted by a federal law, the Depository Institutions Deregulation  
4 and Monetary Control Act of 1980 ("DIDMCA"). The state restriction, known as the California  
5 "per diem" restriction, requires mortgage lenders to make interest-free mortgage loans for  
6 several days after the funds are disbursed by barring the charging of any interest on residential  
7 first mortgages for more than one day prior to the recording of a mortgage deed. The audit  
8 required by the Commissioner, if it proceeds, will cost NCMC in excess of \$4 million dollars.  
9 Plaintiffs will never be able to recover these expenditures if they are ultimately successful on the  
10 merits of this action. In addition, as in *Wells Fargo*, the Commissioner has demanded that  
11 NCMC pay restitution to borrowers for its alleged violations of the California per diem  
12 restriction even though NCMC is lawfully entitled to collect such charges under federal law.

#### 13 STATEMENT OF FACTS

14 A. California Law Provides For State Licensing, Regulation, Supervision,  
15 Examination, And Enforcement Against National Bank Operating  
16 Subsidiaries And Imposes A Per Diem Interest Charge Restriction On  
Mortgages.

17 National City Bank, a national banking association that is organized and exists  
18 under the National Bank Act, 12 U.S.C. § 21 *et seq.*, through NCMC, a wholly owned operating  
19 subsidiary of National City Bank that operates under the National Bank Act and implementing  
20 OCC regulations, makes residential mortgage loans in California. Knight Decl. ¶ 2; Stille Decl.  
21 ¶ 2. Under the California Residential Mortgage Lending Act ("California RMLA"), Cal. Fin.  
22 Code § 50002(a) *et seq.*, "[n]o person shall engage in the business of making residential  
23 mortgage loans or servicing residential mortgage loans, in this state, without first obtaining a  
24 license from the commissioner [of the DOC]," *id.* § 50002(a). Although national banks are  
25 exempt from this requirement under California Financial Code § 50003(g), the terms of the  
26 California RMLA purport to apply to national banks' operating subsidiaries, including NCMC,  
27 that engage in residential mortgage lending in California. NCMC obtained an RMLA license in  
28

1 1997, the year before it became an operating subsidiary of National City Bank. See Knight  
2 Decl. ¶ 6.

3 Under the California RMLA, NCMC may not "[r]equire a borrower to pay  
4 interest on [a] mortgage loan for a period in excess of one day prior to recording of the  
5 mortgage or deed of trust." Cal. Fin. Code § 50204(o). This California per diem restriction  
6 limits to only one day the interest that a residential mortgage lender in California may charge  
7 prior to the recording of the mortgage, even if the time between the disbursement of the  
8 mortgage funds to the consumer and the date on which the mortgage is actually recorded is  
9 longer than one day. Another per diem provision purports to impose a similar restriction on all  
10 residential mortgage lenders, including both National City Bank and NCMC, regardless of  
11 whether they must be licensed under the California RMLA or any other California lending law.  
12 Cal. Civ. Code § 2948.5.

13 The Commissioner has broad authority pursuant to the California RMLA to  
14 enforce the California per diem restriction. "As often as the commissioner deems necessary and  
15 appropriate, but at least once every 48 months," an entity required to be licensed under the  
16 RMLA must allow "the commissioner [to] examine [its] affairs . . . for compliance with" the  
17 RMLA and other applicable laws. Cal. Fin. Code § 50302(a). If the Commissioner finds that a  
18 entity required to hold an RMLA license has committed a violation of any provision of any law  
19 including the California RMLA, that entity is subject to criminal prosecution, revocation of its  
20 license and prohibition on further business activities, censure or suspension of its officers, an  
21 administrative cease and desist order, an injunction, or a restraining order. Cal. Fin. Code  
22 §§ 50315, 50318, 50320 to 50325.

23 B. Congress And The OCC Have Authorized National Banks To Establish  
24 Operating Subsidiaries That Are Subject To The OCC's Exclusive  
25 Licensing, Regulatory, Supervisory, Examination, And Enforcement  
26 Authority.

27 "National banks are created and governed by the National Bank Act. 12 U.S.C.  
28 § 21 *et seq.*" Wells Fargo PI Order at 5 (2003 WL 1220131, at \*2). "The National Bank Act  
was enacted to 'facilitate . . . "a national banking system"' . . . and 'to protect national banks

1 against intrusive regulation by the States.” *Wells Fargo* PI Order at 5-6 (2003 WL 1220131, at  
2 \*2) (citing and quoting *Marquette Nat’l Bank of Minneapolis v. First of Omaha Serv. Corp.*, 439  
3 U.S. 299, 314-15 (1978), and *Bank of America v. City and County of San Francisco*, 309 F.3d  
4 551, 561 (9th Cir. 2002), *cert. pending*, No. 02-1404 (filed March 20, 2003)). Under the  
5 National Bank Act and other federal banking laws, the OCC has exclusive licensing, regulatory,  
6 supervisory, examination, and enforcement authority with respect to national banks’ compliance  
7 with both federal and non-preempted state laws. *See* 12 U.S.C. §§ 24(Seventh), 484(a),  
8 1818(b). Congress has authorized national banks to receive deposits, loan money, and exercise  
9 “all such incidental powers as shall be necessary to carry on the business of banking.” 12  
10 U.S.C. § 24(Seventh).

11 A national bank’s incidental powers under 12 U.S.C. § 24(Seventh) include the  
12 authority to provide banking services through operating subsidiaries. Under an OCC regulation  
13 interpreting § 24(Seventh), codified at 12 C.F.R. § 5.34, national banks are expressly authorized  
14 to establish and own operating subsidiaries, which can conduct only activities that are lawful for  
15 the parent national bank itself. 12 C.F.R. § 5.34(e)(1). The OCC’s operating-subsidary  
16 regulation further provides for prior licensing through application and OCC approval before an  
17 operating subsidiary is established and acquired by a national bank. *See, e.g., id.* § 5.34(e)(5).  
18 The OCC’s operating-subsidary regulation also makes clear that operating subsidiaries are  
19 subject to the OCC’s ongoing supervision, regulation, examination, and enforcement authority.  
20 *See id.* § 5.34(e)(3). *See also Wells Fargo* PI Order at 10 (2003 WL 1220131, at \*5)  
21 (“[o]perating subsidiaries and national banks have been treated as equivalents in court decisions  
22 determining whether a particular activity was permissible for a national bank.”) (citing cases).

23 Given that operating subsidiaries conduct only national bank-authorized  
24 activities, and therefore act as separately incorporated divisions or departments of the national  
25 bank itself, and because operating subsidiaries are subject to ongoing federal licensing,  
26 regulation, supervision, examination, and enforcement by the OCC, the OCC’s regulations  
27 further provide that, “[u]nless otherwise provided by Federal law or OCC regulation, State law  
28

1 apply to national bank operating subsidiaries to the same extent that those laws apply to the  
2 parent national bank." 12 C.F.R. § 7.4006.

3 Under 12 U.S.C. § 484(a), "[n]o national bank shall be subject to any visitorial  
4 powers except as authorized by Federal law, vested in the courts of justice or such as shall be, or  
5 have been exercised or directed by Congress or by either House thereof or by any committee of  
6 Congress or of either House duly authorized." Section 484(b) provides a limited exemption to  
7 this exclusive federal regulatory, supervisory, and examination jurisdiction over national banks,  
8 but only for a state "to ensure compliance with applicable State unclaimed property or escheat  
9 laws upon reasonable cause to believe that the bank has failed to comply with such laws."

10 Interpreting § 484, the OCC's regulations provide that "[o]nly the OCC or an  
11 authorized representative of the OCC may exercise visitorial powers with respect to national  
12 banks, except as provided [in the regulation interpreting 12 U.S.C. § 484(b)]. State officials  
13 may not exercise visitorial powers with respect to national banks, such as conducting  
14 examinations, inspecting or requiring the production of books or records of national banks, or  
15 prosecuting enforcement actions, except in limited circumstances authorized by federal law."  
16 12 C.F.R. § 7.4000(a)(1). The OCC's regulation defines "visitorial powers" to include  
17 "[e]xamination of a bank," "[i]nspection of a bank's books and records," "[r]egulation and  
18 supervision of activities authorized or permitted pursuant to federal banking law," and  
19 "[e]nforcing compliance with any applicable federal or state laws concerning those activities."  
20 *Id.* § 7.4000(a)(2).

21 Both courts and the OCC have interpreted the National Bank Act to provide that  
22 a state cannot require national banks to obtain a license as a condition of doing business in a  
23 state. *Bank of America, Nat'l Trust & Sav. Ass'n v. Lima*, 103 F. Supp. 916, 917-18 (D. Mass.  
24 1952) (citing *First Nat'l Bank in St. Louis v. Missouri*, 263 U.S. 640, 656 (1924)); see also *First*  
25 *Nat'l Bank of Eastern Arkansas v. Taylor*, 907 F.2d 775, 777-78 (8th Cir. 1990); *Ass'n of Bank*  
26 *in Insurance, Inc. v. Duryee*, 55 F. Supp. 2d 799, 812 (S.D. Ohio 1999), *aff'd*, 270 F.3d 397 (6  
27 Cir. 2001); OCC Interpr. Ltr. No. 749 (Sept. 13, 1996), reprinted in [1996-1997 Transfer  
28 Binder] Fed. Banking L. Rep. (CCH) ¶ 81-114 (ApX B); OCC Interpr. Ltr. No. 644 (March 24

1 1994), *reprinted in* [1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,553 (Apx C).  
2 Under 12 C.F.R. § 7.4006, these protections from state licensing, regulation, supervision,  
3 examination, and enforcement also apply to operating subsidiaries of national banks.

4 On February 11, 2003, the First Senior Deputy Comptroller and Chief Counsel of  
5 the OCC sent a letter to the Commissioner confirming that "pursuant to 12 U.S.C. § 484, and 12  
6 C.F.R. §§ 5.34(e)(3) and 7.4006, the OCC has exclusive visitorial authority over national banks  
7 and their operating subsidiaries except where *Federal* law provides otherwise." Apx D, at 2.  
8 The OCC's letter continued: "As a result, States are precluded from examining or requiring  
9 information from national banks or their operating subsidiaries." *Id.* The OCC explained that  
10 "it is well established that a State may not condition a national bank's exercise of a permissible  
11 Federal power on obtaining the State's prior approval, including the imposition of State  
12 licensing requirements as a predicate to the exercise of that power. The result is the same  
13 whether the national bank exercises the power directly, or through an operating subsidiary that  
14 has been licensed by the OCC. In both cases, the bank, or the operating subsidiary, has obtained  
15 a *Federal* license to conduct its business." *Id.* at 6 (emphasis in original). This letter follows  
16 earlier letters issued by the OCC to the same effect.

17 The OCC thereafter filed a brief *amicus curiae* with this Court in the virtually  
18 identical *Wells Fargo* case (No. 03-0157 GEB JFM), confirming that operating subsidiaries of  
19 national banks are subject to the exclusive visitorial powers of the OCC and states cannot  
20 exercise any licensing, regulatory, supervisory, or enforcement authority over such entities.  
21 Accordingly, the OCC argued in its brief, the Commissioner's attempted exercise of visitorial  
22 powers, and interference with operating subsidiaries' business operations in California, are  
23 preempted.

24 Subsequently, this Court held that "[t]he OCC's *amicus* brief and interpretive  
25 letter appear to be 'both persuasive and consistent with the National Bank Act and OCC  
26 regulations and thus at least 'entitled to respect.'"" *Wells Fargo* PI Order at 12 (2003 WL  
27 1220131, at \*6) (quoting *Bank of America*, 309 F.3d at 563 n.7).  
28



1           C.     **Congress Has Expressly Preempted State Limitations On Mortgage Interest**  
2                   **Charges In DIDMCA.**

3                   Under the federal Depository Institutions Deregulation and Monetary Control  
4           Act of 1980 or "DIDMCA," "[t]he provisions of the constitution or laws of any State expressly  
5           limiting the rate or amount of interest, discount points, finance charges, or other charges which  
6           may be charged, taken, received, or reserved shall not apply to any loan, mortgage, credit sale,  
7           or advance which is" (a) "secured by a first lien on residential real property"; (b) "made after  
8           March 31, 1980"; and (c) a "federally related mortgage loan," i.e., a loan that is secured by  
9           residential real property and is made by a party who qualifies as a "creditor" under the Truth In  
10          Lending Act, 15 U.S.C. § 1602(f), and who makes residential real estate loans aggregating more  
11          than \$1 million per year. 12 U.S.C. § 1735f-7a(a)(1); 12 U.S.C. § 1735f-5(b)(1) and (2)(D).

12                  DIDMCA allowed states to override this express preemption of state limits on  
13          mortgage interest and fees, but states were required to exercise this authority prior to April 1,  
14          1983, and to make explicit reference when they did so to 12 U.S.C. § 1735f-7a(a)(1). California  
15          did not opt out of this provision of DIDMCA within the specified time period.

16                               **ARGUMENT**

17                  "Traditionally, a court may issue a preliminary injunction if it determines:  
18          (1) the moving party will suffer irreparable injury if the relief is denied; (2) the moving party  
19          will probably prevail on the merits; (3) the balance of potential harm favors the moving  
20          party; and, depending on the nature of the case, (4) the public interest favors granting relief."  
21          *International Jensen, Inc. v. Metrosound U.S.A., Inc.*, 4 F.3d 819, 822 (9th Cir. 1993) (citation  
22          omitted). As this Court held in *Wells Fargo*, the Ninth Circuit has also adopted an "alternative  
23          standard" under which the moving party may meet its burden by "demonstrat[ing] either: '(1) a  
24          combination of probable success on the merits and the possibility of irreparable injury if relief is  
25          not granted; or (2) the existence of serious questions going to the merits and that the balance of  
26          hardships tips sharply in its favor.'" *Wells Fargo* PI Order at 4 (2003 WL 122031, at \*2)

1 (quoting *Int'l Jensen*, 4 F.3d at 822).<sup>2</sup> In this case, Plaintiffs easily meet either the "traditional"  
2 or the "alternative" standard because they can establish a probable success on the merits,  
3 substantial irreparable harm if relief is denied, and a balance of equities that tips sharply in their  
4 favor.

5 **I. PLAINTIFFS ARE LIKELY TO SUCCEED ON THE MERITS.**

6 This motion presents pure issues of law: (1) Whether a state requirement that  
7 national banks' operating subsidiaries must be licensed, regulated, supervised, examined, and  
8 subject to enforcement actions by state authorities is valid given federal law which expressly  
9 vests exclusive authority over such matters in the OCC? And (2) whether California's  
10 enforcement of a state law limiting the charging of interest on residential mortgage loans to one  
11 day prior to recording of the mortgage is expressly preempted by a federal law allowing the  
12 charging of such interest? The governing legal principles are well established and compel the  
13 conclusion that the Plaintiffs are likely to succeed on the merits of their claim that the California  
14 laws at issue are preempted.

15 **A. The Commissioner's Assertion Of Licensing, Supervisory, Regulatory,  
16 Examination, and Enforcement Authority Over National Bank Operating  
17 Subsidiaries Is Preempted By The OCC's Exclusive Visitorial And Licensing  
18 Powers.**

19 The OCC has exclusive visitorial authority over national banks. See 12 U.S.C.  
20 § 484(a) ("No national bank shall be subject to any visitorial powers except as authorized by  
21 Federal law, vested in the courts of justice or [as directed by Congress.]").<sup>3</sup> As this Court

22 <sup>2</sup> Under the Ninth Circuit's "alternative standard" for preliminary relief, the court uses a  
23 sliding scale in deciding whether a preliminary injunction is warranted: "[T]he greater the  
24 relative hardship to the moving party, the less probability of success must be shown." *National  
25 Ctr. for Immigrants Rights, Inc. v. INS*, 743 F.2d 1365, 1369 (9th Cir. 1984). Alternatively, if  
26 the probability of success on the merits is very high, then the amount of irreparable harm that  
27 need be shown is lessened. Thus, the amount of irreparable harm that must be shown is  
28 inversely proportional to the likelihood of success on the merits. *Sun Microsystems, Inc. v.  
Microsoft Corp.*, 188 F.3d 1115, 1119 (9th Cir. 1999).

29 <sup>3</sup> See also *National State Bank v. Long*, 630 F.2d 981, 989 (3d Cir. 1980) (explaining that  
30 "exclusivity of the [OCC's] power to examine [for compliance with legal requirements] is a  
31 reasonable interpretation of the National Bank Act"); OCC Interpretive Letter No. 614 [1992-  
32 1993 Transfer Binder] Fed. Banking L. Rep. ¶ 83,454 (Jan. 15, 1993) ("[T]he Office of  
33 (continued...)")

1 observed in the *Wells Fargo* PI Order, "the term "visitorial" powers as used in section 484  
2 generally refers to the power of the OCC to "visit" a national bank to examine its activities and  
3 its observance of applicable laws, and encompasses any examination of a national bank's  
4 records relative to the conduct of its banking business as well as any enforcement action that  
5 may be undertaken for violations of law." *Wells Fargo* PI Order at 5 n.3 (2003 WL 1220131, at  
6 \*2 n.3) (quoting OCC PI Amicus Br. 2-3).<sup>4</sup> As noted above, the OCC's regulation defines  
7 "visitorial powers" to include "[e]xamination of a bank"; "[i]nspection of a bank's books and  
8 records"; "[r]egulation and supervision of activities authorized or permitted pursuant to federal  
9 banking law"; and "[e]nforcing compliance with any applicable federal or state laws concerning  
10 those activities." 12 C.F.R. § 7.4000(a)(2).

11 Following this long line of cases, the OCC's regulations provide that "[o]nly the  
12 OCC or an authorized representative of the OCC may exercise visitorial powers with respect to  
13 national banks," and that "State officials may not exercise visitorial powers with respect to  
14 national banks, such as conducting examinations, inspecting or requiring the production of  
15 books or records of national banks, or prosecuting enforcement actions, except in limited  
16 circumstances authorized by federal law." 12 C.F.R. § 7.4000(a)(1).

17 The courts also have held that a state cannot subvert these restrictions by  
18 requiring national banks to obtain a license in order to do business in that state. National banks  
19 are "instrument[s] of the national government," whose "presence in the state is attributable to  
20 the national power, not to the state's permission." *Bank of America, Nat'l Trust & Sav. Ass'n v.*  
21 *Lima*, 103 F. Supp. 916, 917-18 (D. Mass. 1952) (citing *First Nat'l Bank in St. Louis v.*  
22 *Missouri*, 263 U.S. 640, 656 (1924)). As a result, "any attempt by the state to block [a national

23 Comptroller of the Currency has consistently maintained that state attempts to exercise  
24 supervisory authority over national banks are preempted.") (Apex E).

25 <sup>4</sup> Visitation "is a . . . power to control and arrest abuses, and to enforce a due observance  
26 of the statutes [by the regulated entity]." *Allen v. McKean*, 1 F. Cas. 489, 498 (C.C.D. Mc.  
27 1833); accord *State v. First National Bank*, 123 P. 712, 715 (Or. 1912) (applying the same  
28 definition to the predecessor of 12 U.S.C. § 484).

1 bank's] entry until it complied with certain conditions would violate the constitution and laws of  
2 the United States." *Id.* at 918; see also *First Nat'l Bank of Eastern Arkansas v. Taylor*, 907 F.2d  
3 775, 777-78 (8th Cir. 1990); *Ass'n of Banks in Insurance, Inc. v. Duryee*, 55 F. Supp. 2d 799,  
4 812 (S.D. Ohio 1999) (finding that licensing and registration schemes applied to national banks  
5 constitute "impermissible conditions upon the ability of a national bank to do business within  
6 the state"), *aff'd*, 270 F.3d 397 (6th Cir. 2001).

7 A necessary corollary to the rule that a state may not require a national bank to  
8 be licensed before the bank conducts business activities in a state is that the state may not  
9 subject national banks to state enforcement actions if they operate without such licenses. In  
10 *First Nat'l Bank of Eastern Arkansas*, the Eighth Circuit so held, refusing to allow a state  
11 regulator to prevent an unlicensed national bank from offering financial products connected to  
12 the bank's lending activities. 907 F.2d at 777-78. "Because national banks are considered  
13 federal instrumentalities," the court of appeal explained, "states may neither prohibit nor unduly  
14 restrict their activities." *Id.* at 778 (citations omitted). Accordingly, it is well established as a  
15 matter of federal law that state laws that purport to require national banks to be licensed by a  
16 state in order to engage in banking activities within the state are preempted by federal law.<sup>5</sup>

17 Under governing federal regulations, these protections from state licensing,  
18 regulation, supervision, examination, and enforcement apply to the operating subsidiaries of  
19 national banks as well as to national banks themselves. Specifically, OCC regulation 12 C.F.R.  
20 § 5.34 provides that national banks may establish, own, and operate operating subsidiaries to  
21 undertake those activities that are authorized for a national bank itself (and only those

22 <sup>5</sup> The OCC has likewise confirmed in interpretive letters that state laws requiring national  
23 banks to be licensed, registered, or to pay registration fees are preempted by federal law. For  
24 example, in 1996, the OCC opined that a state law that required a national bank to be licensed  
25 by a state before it could sell annuities in the state was preempted by federal law. See OCC  
26 Interpr. Ltr. No. 749 (Sept. 13, 1996), reprinted in [1996-1997 Transfer Binder] Fed. Banking  
27 L. Rep. (CCH) ¶ 81-114 (Apx B). In 1994, the OCC found that state registration and licensing  
28 fee requirements imposed on national-bank mortgage lenders were preempted by federal law.  
See OCC Interpr. Ltr. No. 644 (March 24, 1994), reprinted in [1994 Transfer Binder] Fed.  
Banking L. Rep. (CCH) ¶ 83,553 (Apx C).

1 activities). This regulation also provides that an operating subsidiary is subject to ongoing  
2 licensing, regulatory, supervisory, examination, and enforcement authority by the OCC with  
3 respect to its compliance with both federal and non-preempted state laws. And OCC regulation  
4 12 C.F.R. § 7.4006 further prescribes that "[u]nless otherwise provided by Federal law or OCC  
5 regulation, State laws apply to national bank operating subsidiaries to the same extent that those  
6 laws apply to the parent national bank." Accordingly, an operating subsidiary is subject to the  
7 same exclusive licensing, regulatory, supervisory, examination, and enforcement powers of the  
8 OCC as a national bank itself, with respect to its compliance with both federal and non-  
9 preempted state laws; and such subsidiary is not subject to such licensing, regulation,  
10 supervision, examination, and enforcement powers of a state regulator like the Commissioner.

11 The OCC's interpretative letters and *amicus* brief discussed above, p. 6,  
12 expressly confirm this interpretation of the National Bank Act and the OCC's regulations. As  
13 this Court found in *Wells Fargo*, the OCC's interpretation of the National Bank Act and its  
14 regulations is entitled to substantial deference: "The OCC's *amicus* brief and interpretive letter  
15 appear to be 'both persuasive and consistent with the National Bank Act and OCC regulations  
16 and thus at least 'entitled to respect.'"" *Wells Fargo* PI Order at 12 (2003 WL 1220131, at \*6)  
17 (quoting *Bank of America*, 309 F.3d at 563 n.7). The Supreme Court in *United States v. Mead*  
18 *Corp.*, 533 U.S. 218, 231 n.13 (2001), stated that "longstanding precedent conclud[es] that  
19 '[t]he Comptroller of the Currency is charged with the enforcement of banking laws to an extent  
20 that warrants the invocation of [the rule of *Chevron* deference - i.e., that which is commanded  
21 by *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984)] with  
22 respect to his deliberative conclusions as to the meaning of these laws'" (quoting *NationsBank*  
23 *of N.C., N.A. v. Variable Annuity Life Ins. Co.*, 513 U.S. 251, 256-57 (1995)). *Mead* expressly  
24 approved the Court's prior determination in *NationsBank* that the OCC's interpretive letters  
25 receive full *Chevron* deference. *Mead*, 533 U.S. at 231 & n.13; see also *Bank of America*, 309  
26 F.3d at 563 n.7; *Wells Fargo Bank Texas, N.A. v. James*, 321 F.3d 488 (5th Cir. 2003).

27 Furthermore, in *Christensen v. Harris County*, 529 U.S. 576, 588 (2000), the  
28 Court acknowledged "that an agency's interpretation of its own regulation is entitled to

1 deference" unless the language of the regulation unambiguously points in the other direction,  
2 and cited *Auer v. Robbins*, 519 U.S. 452, 461 (1997). Thus, in light of the OCC's recent letters  
3 confirming both national banks' authority to establish, own, and operate operating subsidiaries  
4 and the OCC's exclusive regulation, supervision, examination, and enforcement powers over  
5 those operating subsidiaries, there should be no doubt that national banks are authorized by the  
6 National Bank Act and OCC regulations to establish and own operating subsidiaries that are  
7 subject to the OCC's exclusive authority with respect to their permissible activities, including  
8 mortgage lending activities.

9 State and local laws are preempted under the Supremacy Clause, U.S. CONST.  
10 art. VI, when they "stand[] as an obstacle to the accomplishment and execution of the full  
11 purposes and objectives of Congress." *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941) (citation  
12 omitted); accord *Bank of America*, 309 F.3d at 561; *American Bankers Ass'n v. Lockyer*, 239  
13 F. Supp. 2d 1000, 1008 (E.D. Cal. 2002). Moreover, "[f]ederal regulations have no less pre-  
14 emptive effect than federal statutes." *Fidelity Federal Savings & Loan Ass'n v. de la Cuesta*,  
15 458 U.S. 141, 153 (1982). The California RMLA, which purports to subject national banks'  
16 operating subsidiaries like NCMC to ongoing licensing, regulation, supervision, examination,  
17 and enforcement by the Commissioner – in this case through the Commissioner's demands to  
18 enforce the California per diem restriction against NCMC – violates the exclusive federal  
19 licensing, regulatory, supervisory, examination, and enforcement powers of the OCC. Those  
20 state laws are therefore preempted under the Supremacy Clause.

21 In sum, under federal law, the OCC is the exclusive enforcer of non-preempted  
22 state laws against national banks as well as their operating subsidiaries. And NCMC, as an  
23 operating subsidiary of a national bank, need not hold a license under the California RMLA in  
24 order to engage in the residential mortgage lending and servicing business in California.

25 **B. The California RMLA Is Preempted Because It Conflicts With A National**  
26 **Bank's Powers To Establish And Own Operating Subsidiaries.**

27 National banks have authority under the National Bank Act to receive deposits,  
28 loan money, and exercise "all such incidental powers as shall be necessary to carry on the

1 business of banking." 12 U.S.C. § 24(Seventh). The OCC's regulations implementing the  
2 National Bank Act provide that national banks are expressly authorized to establish and own  
3 operating subsidiaries, which can conduct only those activities that are lawful for the national  
4 bank itself. 12 C.F.R. § 5.34(e)(1). The OCC's regulations further provide that a national  
5 bank's operating subsidiary may exercise the national bank's enumerated federal lending and  
6 incidental powers to engage in the "business of banking" under 12 U.S.C. § 24(Seventh) on the  
7 same basis as the national bank. See 12 C.F.R. §§ 5.34(e)(1), 7.4006.

8 The National Bank Act's "grants of both enumerated and incidental 'powers' to  
9 national banks" are "not normally limited by, but rather ordinarily pre-empt[], contrary state  
10 law." *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25, 32 (1996) (unanimous  
11 opinion). This view of the National Bank Act was recently reiterated by the Ninth Circuit in  
12 *Bank of America*, 309 F.3d at 558-59, which struck down local ATM fee ban ordinances  
13 because they interfered with national banks' "incidental powers" under § 24(Seventh), as  
14 interpreted by OCC regulations. The same view was reiterated by this Court in *American*  
15 *Bankers Association v. Lockyer*, 239 F. Supp. 2d at 1012-13, in which Judge Damrell struck  
16 down a California statute imposing disclosure obligations on national banks' credit card  
17 repayment terms.

18 The long-standing approach to preemption of state laws that interfere with  
19 national banks' authorized powers recognizes that national banks are "instrumentalities of the  
20 federal government . . . and as such [are] necessarily subject to the paramount authority of the  
21 United States." *Davis v. Elmira Sav. Bank*, 161 U.S. 275, 283 (1896). Moreover, the Supreme  
22 Court reaffirmed the proposition that "an 'assumption' of nonpre-emption is *not* triggered when  
23 the State regulates in an area where there has been a history of significant federal presence."  
24 *United States v. Locke*, 529 U.S. 89, 108 (2000) (emphasis added) (citing and quoting *Jones v.*  
25 *Rath Packing Co.*, 430 U.S. 519, 525 (1977)). This "assumption" is triggered where "the field  
26 which Congress is said to have pre-empted has been traditionally occupied by the States."  
27 *Jones*, 430 U.S. at 525; accord *Locke*, 529 U.S. at 108. By contrast, the history of preemption  
28 of state law purporting to regulate federally chartered banks reaches back to the beginnings of

1 the Republic. See *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 326 (1819). Without  
2 question, "there has been a history of significant federal presence" in national bank regulation,  
3 and the regulation of national banks' authorized activities has *never* been an area "traditionally  
4 occupied by the States."

5 A state law is preempted where it "prevent[s] or significantly interfere[s] with  
6 the national bank's exercise of its powers." *Barnett Bank*, 517 U.S. at 33 (citations omitted)  
7 (emphasis added).<sup>6</sup> "[W]here Congress has not expressly conditioned the grant of 'power' [to  
8 national banks] upon a grant of state permission, the Court has ordinarily found that no such  
9 condition applies." *Id.* at 34 (emphasis added); *Franklin National Bank of Franklin Square v.*  
10 *New York*, 347 U.S. 373, 378 & n.7 (1954) ("We find no indication that Congress intended to  
11 make this phase of national banking subject to local restrictions, as it has done by express  
12 language in several other instances.").

13 The Commissioner's enforcement of the California RMLA prevents and  
14 significantly interferes with the power of National City Bank, a national bank, to conduct – and  
15 exercise its choice to conduct – its activities through an operating subsidiary, as authorized by  
16 the National Bank Act and OCC regulations adopted pursuant to that Act. And California law  
17 by seeking to impose ongoing state regulation, supervision, examination, and enforcement also  
18 imposes additional impediments and burdens on National City Bank's exercise of its federal  
19 lending powers to the extent it chooses to use an operating subsidiary. National City Bank does  
20 not face these impediments if it exercises its powers only within the bank itself. As a result,  
21 under the Supreme Court's decision in *Barnett Bank* and the Ninth Circuit's recent decision in  
22 *Bank of America*, the California RMLA, Cal. Fin. Code § 50002 *et seq.*, as enforced by the

23 <sup>6</sup> Moreover, *Barnett Bank*, 517 U.S. at 33, recognized that a "federal regulation  
24 permitting, but not requiring, national banks to" use a certain clause in a mortgage contract "pre-  
25 empts a state law forbidding the use of such a clause," citing *Fidelity Federal Savings & Loan*  
26 *Ass'n*, 458 U.S. at 153 ("Federal regulations have no less pre-emptive effect than federal  
27 statutes."). Here, § 5.34 of the OCC's regulations permits, but does not require, National City  
28 Bank, as a national bank, to establish, own, and conduct its authorized mortgage lending and  
servicing activities through an operating subsidiary.



1 Commissioner, both prevents and significantly interferes with National City Bank's exercise of  
2 its express lending power and of its incidental power to lend through an operating subsidiary  
3 pursuant to 12 C.F.R. §§ 5.34, 7.4000, and 7.4006. Accordingly, these state laws are preempted  
4 under Article VI of the United States Constitution.

5 C. The California Per Diem Interest Charge Restriction Is Expressly  
6 Preempted By DIDMCA.

7 In *Wells Fargo*, this Court concluded that it did not need to reach Plaintiffs'  
8 DIDMCA claim in order to grant the motion for a preliminary injunction. As in *Wells Fargo*,  
9 however, the law that is at the heart of this dispute – the California per diem restriction – is  
10 preempted by DIDMCA.

11 "Congress enacted DIDMCA to promote the stability and viability of financial  
12 institutions by allowing them to charge market interest on mortgage loans, and to promote home  
13 ownership by increasing the flow of available mortgage money." *Brown v. Investors Mortgage*  
14 *Co.*, 121 F.3d 472, 475 (9th Cir. 1997) (per curiam). Under DIDMCA, "[t]he provisions of the  
15 constitution or laws of any State expressly limiting the rate or amount of interest, discount  
16 points, finance charges, or other charges which may be charged, taken, received, or reserved  
17 shall not apply to any loan, mortgage, credit sale, or advance which is" (a) "secured by a first  
18 lien on residential real property"; (b) "made after March 31, 1980"; and (c) a "federally related  
19 mortgage loan." 12 U.S.C. § 1735f-7a(a)(1); 12 U.S.C. § 1735f-5(b)(1) and (2)(D).<sup>7</sup>

20 In enacting DIDMCA, Congress provided that individual States could override  
21 this express preemption provision, but only if they did so prior to April 1, 1983, and only if they  
22

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23 <sup>7</sup> A "federally related mortgage loan" is defined in 12 U.S.C. § 1735f-5(b), as modified b  
24 DIDMCA in § 1735f-7a(a)(1). Such a loan for purposes of DIDMCA preemption is one that is  
25 secured by residential real property and is made by a "creditor," i.e., one who is defined as a  
26 "creditor" under the Truth In Lending Act, 15 U.S.C. § 1602(f), and who makes residential rea  
27 estate loans aggregating more than \$1 million per year. NCMC is a "creditor" under the Truth  
28 In Lending Act, i.e., subject to the Truth In Lending Act's requirements. NCMC makes  
residential real estate loans aggregating more than \$1 million per year. Knight Decl. ¶ 4.

1 made explicit reference to 12 U.S.C. § 1735f-7a(a)(1). California did not exercise its right to  
2 opt out of DIDMCA's express preemption provision.

3 In this case, the mortgages that NCMC makes are first liens secured by  
4 residential real property made after March 31, 1980. Knight Decl. ¶ 4. Its loans are also  
5 "federally related mortgage loans" for purposes of DIDMCA. See *supra* n.7. Accordingly,  
6 NCMC's mortgages are subject to DIDMCA's express preemption clause.

7 The California per diem restriction bars the charging of any interest on a  
8 mortgage loan until one day prior to the recording of the mortgage, even if the funds have been  
9 disbursed to the borrower for several days. This requirement that NCMC make interest-free  
10 mortgage loans for several days is a state "provision[] . . . expressly limiting the . . . amount of  
11 interest" charged on residential first mortgage loans by a lender covered by DIDMCA's  
12 preemption clause and therefore is expressly preempted under 12 U.S.C. § 1735f-7a(a)(1).

13 In *Shelton v. Mutual Savings & Loan Ass'n, F.A.*, 738 F. Supp. 1050, 1056-58  
14 (E.D. Mich. 1990), the court held a Michigan statute that prohibited residential mortgage lenders  
15 from charging interest on first mortgage loans *before disbursement* to be preempted by  
16 DIDMCA. If a state law that prohibits the charging of interest *before* mortgage funds are  
17 disbursed is preempted, then *a fortiori* a statute that prohibits the charging of interest *after* funds  
18 are disbursed is preempted. See also *Brown*, 121 F.3d at 475 (finding Washington's usury  
19 statute "plainly" preempted for first mortgages, and finding that the purposes of DIDMCA  
20 would not be served by limiting the plain language of DIDMCA's preemption provision).

21 There is no basis for the Commissioner's contention in the related cases of *Wells*  
22 *Fargo and Quicken Loans, Inc. v. Boutris*, No. 03-0256 GEB JFM, that "[a]n analogy may be  
23 drawn between [the] California [per diem restriction] and the simple interest statute (SIS) which  
24 is not preempted by DIDMCA according to the appellate court in *Grunbeck v. Dime Savings*  
25 *Bank of New York, FSB*, 74 F.3d 331 (1st Cir. 1996)." *Wells Fargo PI Opp.* at 12. There is a  
26 crucial difference between this case and *Grunbeck*. In *Grunbeck*, the court held that "[t]he SIS  
27 leaves entirely to the parties the rate and amount of simple interest to be exacted." 74 F.3d at  
28 337. Here, in contrast, the per diem interest restriction does *not* "leave entirely to the parties th